No. 87-654

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

NEW ENERGY COMPANY OF INDIANA,
Appellant,

v.

JOANNE LIMBACH,
TAX COMMISSIONER OF OHIO, MARY ELLEN WITHROW,
TREASURER OF OHIO, AND SOUTH POINT ETHANOL,
Appellees.

On Appeal from the Supreme Court of Ohio

**BRIEF OF THE
NATIONAL GOVERNORS' ASSOCIATION,
INTERNATIONAL CITY MANAGEMENT ASSOCIATION,
NATIONAL CONFERENCE OF STATE LEGISLATURES,
NATIONAL ASSOCIATION OF COUNTIES,
COUNCIL OF STATE GOVERNMENTS,
U.S. CONFERENCE OF MAYORS, AND
NATIONAL LEAGUE OF CITIES
AS *AMICI CURIAE* IN SUPPORT OF APPELLEES**

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QUESTION PRESENTED

Whether Ohio's credit against its fuel sales tax for gasohol—which applies only to fuel containing ethanol produced in Ohio or in other States providing a reciprocal tax credit for ethanol produced in Ohio—is valid under the Commerce Clause.

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INTEREST OF THE *AMICI CURIAE*

The *amici*, organizations whose members include state, county, and municipal governments and officials throughout the United States, have a compelling interest in legal issues that affect state and local governments.

This case presents a Commerce Clause challenge to an Ohio statute that provides a tax credit to fuel dealers who sell gasohol, which is gasoline mixed with ethanol. Ethanol is an alternative to lead, which is a serious pollutant, as an additive to petroleum products. The credit is available for ethanol produced in Ohio or in any other State that provides a similar fuel tax credit for ethanol produced in Ohio.

Appellant New Energy Company of Indiana ("New Energy") invokes the dormant Commerce Clause as a basis for invalidating Ohio's attempt to encourage a substitute for lead in order to improve the environment of the State's citizens. New Energy argues that the Ohio law burdens and discriminates against interstate commerce by placing some interstate businesses (specifically its own) at a competitive disadvantage.

The Supreme Court of Ohio rejected appellant's claim that the tax credit violates the Commerce Clause. In upholding the reciprocity provision of the Ohio statute, the court concluded that "[i]t does not give an advantage solely to Ohio producers, and does not interfere with the flow of ethanol into Ohio by out-of-state suppliers" (J.S. App. 7a). *Amici* submit that the court's opinion strikes the proper balance between the Commerce Clause's proscription against oppressive burdens upon interstate commerce and the State's power to regulate even-handedly to effectuate a legitimate local public purpose.

The dormant Commerce Clause interdicts state legislation that discriminates against or burdens interstate commerce. It has been invoked to invalidate state taxes that fall more heavily on out-of-state businesses. The challenge here, by contrast, is to an Ohio law that imposes no barrier to the flow of commerce into the State and no tax on the importation of ethanol from outside the State. On the contrary, Ohio offers a tax credit to retailers of fuel containing ethanol that is produced

within the State or in other States that afford a reciprocal tax credit for Ohio-produced ethanol. The Ohio tax credit is comparable to a credit against a use tax for sales tax that has been paid, which is provided on a reciprocal basis by most States (*see Williams v. Vermont*, 472 U.S. 14, 21-22 (1985)), and whose validity has not been questioned under the Commerce Clause.

The Ohio tax credit at issue here is a subsidy designed to further the State's interest in a clean environment. It seeks to effectuate that purpose in two ways: by promoting the local production of ethanol to replace lead in motor fuel and by encouraging other States to provide similar incentives to the same end. The statute is an example of the kind of creative experiment that is made possible by the separate sovereign existence of the States. This Court has held that the Commerce Clause does not obligate a State that provides a subsidy to foster commerce to extend that subsidy to out-of-state concerns. *E.g., Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976).

In our view, the Commerce Clause should not be invoked to preserve the profit potential of a single business engaged in interstate commerce at the expense of Ohio's effort to cleanse its environment for the benefit of the health and safety of its citizens. The Commerce Clause protects interstate commerce, not particular interstate businesses.

Amici submit that the decision of the Ohio Supreme Court is correct. Because this Court's decision will have a direct effect on matters of prime importance to *amici* and their members, *amici* submit this brief to assist the Court in its resolution of the case.[1]

[1] Pursuant to Rule 36 of the Rules of the Court, the parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

STATEMENT OF THE CASE

Amici agree with the statements of the case set forth in the briefs of appellees Limbach and South Point Ethanol, but wish to emphasize the following points.

As originally enacted in 1981, the Ohio statute granted motor vehicle fuel dealers a credit against sales tax with respect to the sale of gasohol, which is gasoline containing not more than ten percent by volume of ethanol. Effective January 1, 1985, Ohio amended its statute to provide that fuel eligible for the credit shall not contain ethanol produced outside Ohio unless the producing State "also grants an exemption, credit or refund from such state's motor vehicle fuel excise tax or sales tax for similar fuel containing ethanol produced in Ohio . . . ." Ohio Rev. Code Ann. § 5735.145(B) (Page 1984).

More than 30 States allow sales tax credits for gasohol (J.S. App. 45a). In addition to Ohio, nine States, including the neighboring States of Illinois, Tennessee, and Kentucky, provide that credit only to producers in States that have reciprocal tax credit provisions. Indeed, Indiana, where appellant New Energy operates, had a reciprocal tax credit which was repealed shortly after the State adopted a direct subsidy program in 1984 (J.S. App. 8a, 45a).

Ethanol and gasohol sold in Ohio are obtained primarily through interstate commerce from Illinois and Tennessee (J.S. App. 9a). The record establishes that if New Energy's sales to Ohio dealers are reduced, the primary beneficiaries would be Illinois and Tennessee producers of ethanol (J.S. App. 46a). As the president and chief executive officer of New Energy acknowledged, an Illinois producer (Archer Daniels Midland) would be fully capable of supplying any Ohio markets that New Energy might relinquish (J.A. 79).

SUMMARY OF ARGUMENT

A. To promote a cleaner environment by reducing the use of lead-based pollutants, Ohio grants a special sales tax credit to fuel dealers who sell gasohol, a mixture of gasoline and ethanol. The credit is available for ethanol produced either in Ohio or in other States that provide a similar tax credit for ethanol produced in Ohio.

The Ohio statute satisfies the standard established by this Court in *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), for valid state action under the Commerce Clause. Here, any burden imposed on interstate commerce by the reciprocal tax credit is not excessive in relation to the local benefits that it seeks to achieve. Indeed, the Ohio statute does not prohibit the interstate flow of ethanol but simply conditions out-of-state producers' eligibility for a tax credit on their States' granting Ohio producers comparable treatment. The net effect of this reciprocity provision is disadvantageous to a single Indiana producer, appellant New Energy, because Indiana has repealed its tax credit in favor of a direct subsidy program. But even after the enactment of the Ohio reciprocal tax credit, there continues to be a thriving interstate market for ethanol sold in Ohio, principally from Illinois and Tennessee producers. This Court has held that "interstate commerce is not subjected to an impermissible burden simply because an otherwise valid regulation causes some business to shift from one interstate supplier to another." *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 127 (1978). "[T]he Commerce Clause protects the interstate market, not particular interstate firms, from prohibitive or burdensome regulations" (*id.* at 127-128).

Moreover, the Ohio legislature was amply justified in enacting the reciprocal tax credit to encourage the use of ethanol in surrounding States as a means of clean-

ing the local environment. In these circumstances, the Ohio statute satisfies the *Pike v. Bruce Church* test because it "regulates evenhandedly to effectuate a legitimate local public interest," "its effects on interstate commerce are only incidental," and the burden imposed on interstate commerce is not "excessive in relation to the putative local benefits" (397 U.S. at 142).

B. The Ohio tax credit is not limited to domestic ethanol producers at the expense of out-of-state producers. Indeed, the continued presence of Illinois and Tennessee producers in the Ohio market confirms that Ohio has not erected a discriminatory trade barrier that might implicate the Commerce Clause, and there is no basis for New Energy's speculative allegation that the effect of the Ohio tax statute would cause Ohio-produced ethanol to acquire a larger share of the Ohio market. "The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce." *Exxon*, 437 U.S. at 126 (footnote omitted). The cases upon which New Energy relies are therefore distinguishable because they all involve absolute barriers to interstate commerce.

In practical effect, the Ohio reciprocal tax credit is comparable to the credits against use taxes for sales taxes or against income taxes paid to another State. *See Williams v. Vermont*, 472 U.S. 14, 21-22 (1985). It has never been suggested that such reciprocity violates the Commerce Clause.

C. The Court has held that "[n]othing in the purposes animating the Commerce Clause prohibits a State . . . from participating in the market and exercising the right to favor its own citizens over others." *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 810 (1976) (footnote omitted). That case acknowledged the State's freedom from Commerce Clause restraints in providing a subsidy for commerce that was created by the State. Since that decision, the market participant immunity has been recognized in the context of the sale of commodities and in employment, spheres of commerce in which private parties also operate. This case falls squarely within the original doctrine, for it is undisputed that commerce in ethanol owes its existence to the federal and state tax credits that are provided to gasoline dealers.

The Ohio tax credit is indistinguishable from the subsidy upheld in *Alexandria Scrap*. "Both tax exemptions and tax deductibility are a form of subsidy that is administered through the tax system." *Regan v. Taxation With Representation of Washington*, 461 U.S. 540, 544 (1983); *see also Arkansas Writers Project, Inc. v. Ragland*, 107 S.Ct. 1722, 1730-1732 (1987) (Scalia, J., dissenting). The fact that Ohio did not exercise its prerogative at the outset to limit the tax credit to ethanol from States offering a similar tax credit to Ohio-produced ethanol does not limit Ohio's power to impose that requirement now. *See Alexandria Scrap*, 426 U.S. at 809. Nor is the reciprocity requirement invalid as an initial matter, for the tax credit, like the subsidy in *Alexandria Scrap*, is largesse that Ohio is not constitutionally required to extend to all out-of-state producers.

ARGUMENT

THE OHIO TAX CREDIT PROVISION IS VALID UNDER THE COMMERCE CLAUSE.

A. The Burden Imposed On Interstate Commerce By The Ohio Tax Credit Is Not Excessive In Relation To Local Benefits.

In recent years, the Court has generally used the balancing test enunciated in *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), to determine whether a state law burdens interstate commerce in violation of the Commerce Clause. As the Court there stated (*id.* at 142):

> Where [a] statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.

See Brown-Forman Distillers Corp. v. New York State Liquor Authority, 106 S.Ct. 2080, 2084 (1986); *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Comm'n*, 461 U.S. 375, 393-394 (1983). The Ohio reciprocal tax credit clearly satisfies this standard and therefore does not impermissibly burden interstate commerce.[2]

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[2] *Amici* have previously argued that the "balancing" component of the *Pike v. Bruce Church* standard that measures whether the burden on interstate commerce imposed by a state statute "is clearly excessive in relation to the putative local benefits" is inappropriate and should be discarded. See Brief of the National Governors' Association, *et al.*, as *amici curiae* in *Transcontinental Gas Pipe Line Corp. v. State Oil & Gas Board of Mississippi*, No. 84-1076. The defects inherent in the *Pike v. Bruce Church* stand-

More than 30 States allow tax credits for gasohol (J.S. App. 45a). As the Supreme Court of Ohio found, most of the States near Ohio have reciprocal tax credit provisions (J.S. App. 8a-9a). Indeed, Indiana replaced its reciprocal tax credit with a direct subsidy program. As a result of that action by the Indiana legislature, New Energy, an Indiana ethanol producer, has become ineligible for the Ohio tax credit.[3] But a burden on New Energy is not equivalent to a burden on interstate commerce. As the Ohio Supreme Court observed, "the bulk of ethanol and gasohol sold in Ohio is obtained primarily through interstate commerce, whereby ethanol is shipped into Ohio from Illinois and Tennessee. Thus, New En-

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ard were identified by Justice Scalia in his concurring opinion in *CTS Corp. v. Dynamics Corp. of America*, 107 S.Ct. 1637, 1652-1653 (1987). Undertaking such an analysis of the potential excessiveness of state action in meeting a legitimate state problem (akin to a determination whether the penalty fits the crime) is a policymaking function that belongs more appropriately to the legislative and executive branches than to the courts. Although *amici* believe that the Court's standard for Commerce Clause analysis should be reconsidered, we submit that the Ohio statute unquestionably satisfies the *Pike v. Bruce Church* test.

[3] Indiana replaced its reciprocal tax credit with a direct subsidy for in-state producers like New Energy. Analyzed simply in terms of the effect on out-of-state businesses, a reciprocal credit is far less burdensome than a subsidy limited to in-state producers. Yet this Court has never held that subsidies limited to in-state concerns violate the Commerce Clause. *See generally Arkansas Writers' Project, Inc. v. Ragland*, 107 S.Ct. 1722, 1730-1732 (1987) (Scalia, J., dissenting). Such subsidies frequently represent the essential legislative prerogative to advance the interests of the citizens and businesses in the State. *Amici* submit that there is nothing inherently burdensome about an economic measure labelled a tax credit rather than a subsidy, particularly when it is not limited to in-state producers. The mere fact that the eligibility for the tax credit is conditioned on reciprocity does not create an unconstitutional burden. Such a requirement can be viewed as analogous to a subsidy available to certain businesses but not to others. See also Part C, *infra*, at 16-19.

ergy's inability to compete in the Ohio market will not affect the flow of ethanol through interstate commerce into Ohio gas stations" (J.S. App. 9a). In fact, if New Energy's sales in Ohio are reduced, "the primary beneficiaries would be Illinois and Tennessee producers of ethanol" (*id.* at 46a).

This Court has previously rejected the essence of New Energy's claim of burdensome state regulation. In *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117 (1978), the Court considered a statute that excluded certain out-of-state producers from the retail gasoline market. The Court noted (and the findings confirm that the same is true in this case) that "there is no reason to assume that their share of the entire supply will not be promptly replaced by other interstate refiners" (*id.* at 127). The *Exxon* Court held that "interstate commerce is not subjected to an impermissible burden simply because an otherwise valid regulation causes some business to shift from one interstate supplier to another" (*ibid.*). "[T]he [Commerce] Clause protects the interstate market, not particular interstate firms, from prohibitive or burdensome regulations" (*id.* at 127-128).

As in *Exxon*, the Ohio statute does not implicate the free trade and anti-protectionist values of the Commerce Clause. The tax credit is available to both in-state and out-of-state producers, and the record establishes the continued existence of a thriving interstate market for ethanol sold in Ohio after the enactment of the reciprocal tax credit.

The record also establishes that the tax credit serves a legitimate local purpose. Ethanol is an effective substitute for lead, which is a dangerous atmospheric pollutant. Both the federal government and the States have chosen tax credits as the best means of encouraging the use of ethanol (J.S. App. 39a). In these circumstances, the Ohio legislature was amply justified in enacting the reciprocal tax credit provision to encourage the use of ethanol in surrounding States as a means of cleansing the local environment.[4]

The mere fact that the Ohio legislation may influence the tax policy of other States does not render the statute illegitimate. As the Court recognized in *United States Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 478 (1978), "any time a State adopts a fiscal or administrative policy that affects the programs of a sister State, pressure to modify those programs may result. Unless that pressure transgresses the bounds of the Commerce Clause or the Privileges and Immunities Clause of Art. IV, § 2, see, *e.g.*, *Austin v. New Hampshire*, 420 U.S. 656 (1975), it is not clear how our federal structure is implicated."

Finally, even assuming that the Ohio legislature sought, in part, to protect the Ohio ethanol industry represented by appellee South Point Ethanol from competitive disadvantage (see J.S. App. 63a), that purpose would not invalidate the reciprocal tax credit under the Commerce Clause. *Cf. Henneford v. Silas Mason Co.*, 300 U.S. 577, 581 (1937). In a comparable Equal Protection Clause context, this Court upheld a California tax on insurance companies licensed in States that imposed a higher rate of tax on California insurance companies than California would otherwise impose on those States' insurers doing business in California. *See Western & Southern Life Insurance Co. v. Board of Equalization*, 451 U.S. 648 (1981). In so ruling, the Court, citing

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[4] Whether the Ohio legislation constitutes a sensible means of achieving a clean environment is not at issue. "[I]t is up to legislatures, not courts, to decide on the wisdom and utility of legislation." *Ferguson v. Skrupa*, 372 U.S. 726, 729 (1963). This Court's review under the Commerce Clause is confined to the legitimacy of the purpose.

Pike v. Bruce Church, Inc., 397 U.S. at 143, endorsed the legitimacy of a State's efforts, either through its tax structure or similar reciprocal provisions, to "protect and enhance the reputation" of a domestic industry so that it might compete more effectively in the interstate market (*id.* at 671).

The Ohio tax credit does not go further in protecting in-state commerce. It does not give the in-state producer a competitive advantage over out-of-state producers, such as those from the neighboring States of Illinois and Tennessee.[5] In fact, the in-state producer, appellee South Point, is not the principal beneficiary of the Ohio statute because it does not have the capacity to acquire New Energy's share of the Ohio market (J.A. 28, 76-80, 129). Thus, New Energy's competition is not South Point. Rather, it is ethanol producers in Illinois and Tennessee and gasoline produced without ethanol.

Indeed, it is plain that the Ohio reciprocity provision, standing alone, does not operate to the detriment of New Energy. It is the combination of the reciprocity provision and Indiana's failure to provide reciprocal treatment that makes New Energy ineligible for the Ohio tax credit. Indiana, of course, is free to decide not to offer a reciprocal tax credit for ethanol produced in Ohio or other States. But the Commerce Clause provides no basis for exalting that decision over Ohio's and limiting Ohio's tax and environmental policy choices.

[5] Appellee South Point Ethanol's support of the Ohio reciprocal tax credit is not a basis for invalidating it under the Commerce Clause as protectionist in purpose. This Court has stated in the context of an equal protection challenge that it will not invalidate a state statute "merely because some legislators sought to obtain votes for the measure on the basis of its beneficial side effects on state industry." *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 463 n.7 (1981). In the same case, the Court applied this rule to reject a Commerce Clause challenge. *See id.* at 471 n.15.

B. The Ohio Tax Credit Does Not Discriminate Against Interstate Commerce.

The Ohio tax credit does not affront the core purpose of the Commerce Clause, which is to prevent States from discriminating against interstate commerce by imposing absolute trade barriers or by oppressive taxes. Thus, the Court has struck down state statutes that prohibited the importation of commodities from outside the State (*Philadelphia v. New Jersey*, 437 U.S. 617 (1978)), prohibited out-of-state banks from owning certain interests within the State (*Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27 (1980)), or imposed a higher tax on out-of-state interests compared to in-state interests. *American Trucking Ass'ns, Inc. v. Scheiner*, 107 S.Ct. 2829 (1987); *Tyler Pipe Industries, Inc. v. Washington Dept. of Revenue*, 107 S.Ct. 2810 (1987); *Bacchus Imports, Ltd. v. Diaz*, 468 U.S. 263 (1984); *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984); *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984); *Maryland v. Louisiana*, 451 U.S. 725 (1981); *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318 (1977).

The Ohio reciprocal tax credit at issue in this case does not fit within any of the prohibited categories under this Court's Commerce Clause cases.[6] The Ohio tax credit

[6] In recent years, the Court has analyzed some claims of discrimination under the Commerce Clause by applying a test of "internal consistency." *See American Trucking Ass'ns*, 107 S.Ct. at 2840-2842; *Tyler Pipe Indus.*, 107 S.Ct. at 2820; *Armco*, 467 U.S. at 644-645. This test was first employed in the context of apportionment in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 163 (1983). *Amici* have previously argued that the internal consistency test has no application to a claim of discriminatory taxation under the Commerce Clause. See Brief of the National Governors' Association, *et al.*, as *amici curiae* in *Tyler Pipe Industries, Inc. v. Washington Dept. of Revenue*, Nos. 85-1963,

is not limited to domestic ethanol producers at the expense of out-of-state producers. Both Ohio producers and out-of-state producers are subject to the same treatment. *Cf. Henneford*, 300 U.S. at 581-582. Nor does Ohio bar entry of out-of-state producers to its markets or prohibit the interstate flow of ethanol. Indeed, the continued presence of Illinois and Tennessee producers in the Ohio market confirms that Ohio has not erected any trade barrier that might implicate the Commerce Clause.[7] "The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce." *Exxon*, 437 U.S. at 126 (footnote omitted).

In practical effect, the Ohio reciprocal tax credit is comparable to the credits accorded by 47 States and the District of Columbia against their own use taxes for sales taxes paid to another State.[8] *See Williams v. Vermont*, 472 U.S. 14, 21-22 (1985). It has never been suggested that the requirement of reciprocity violates the Commerce Clause. Quite to the contrary, reciprocity in that comparable context enhances, rather than impedes, interstate commerce.

85-2006. We also suggest that tax credits may not present the same Commerce Clause concerns as taxes. See n.3, *supra*.

Nevertheless, it is clear that a reciprocal tax credit will always pass the internal consistency test. Under that test, " 'the [tax] must be such that, if applied by every jurisdiction,' there would be no impermissible interference with free trade." *Armco*, 467 U.S. at 644, quoting *Container Corp.*, 463 U.S. at 163. If every State offered the same tax credit as Ohio, no claim of discrimination could possibly arise.

[7] There is no basis in the record for New Energy's speculative allegation (Brief 24) that the effect of the Ohio tax credit would cause Ohio producers to acquire a larger share of the Ohio market. *Cf. Exxon Corp. v. Governor of Maryland*, 437 U.S. at 126-127 n.16.

[8] In like fashion, it is common for a State to offer income tax credits to residents of other States on the condition of reciprocal tax treatment of its residents by the other States.

Absent the creation of trade barriers by the Ohio reciprocal tax credit, appellant's reliance upon *Great Atlantic & Pacific Tea Co. v. Cottrell*, 424 U.S. 366 (1976), and *Sporhase v. Nebraska ex rel. Douglas*, 458 U.S. 941 (1982), is misplaced. In *Great Atlantic & Pacific Tea Co.*, the Court, on the authority of *Dean Milk Co. v. Madison*, 340 U.S. 349 (1951), struck down a Mississippi regulation that provided that milk from another State could be sold in Mississippi only if the other State accepted milk processed in Mississippi on a reciprocal basis. Finding that there were no legitimate state interests for the regulation, the Court concluded that "the barrier of the reciprocity clause to sales of out-of-state milk in Mississippi has . . . 'in practical effect exclude[d] from distribution in [Mississippi] wholesome milk produced . . . in [Louisiana]' " (424 U.S. at 375) (citation omitted). A careful reading of the Court's opinion in *Great Atlantic & Pacific Tea Co.* confirms that the critical basis for the ruling was the absolute trade barrier erected by Mississippi. As the Court stated, "Mississippi is not privileged under the Commerce Clause to force its own judgments as to an adequate level of milk sanitation on Louisiana *at the pain of an absolute ban on the interstate flow of commerce in milk*" (*id.* at 380) (emphasis supplied). Here, in marked contrast, Ohio has not barred from its markets any ethanol produced outside the State. *See also Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935).

Sporhase is likewise distinguishable. There, the Court invalidated a Nebraska statute that absolutely forbade export of ground water to another State unless that State granted reciprocal rights to transport its ground water to Nebraska. Because Colorado prohibited the export of its ground water, the reciprocity provision operated as "an explicit barrier to commerce between the two States" (458 U.S. at 957). The reciprocity requirement did not significantly advance Nebraska's legitimate conservation and preservation interests and was therefore invalid.

Again, it is plain that the Court's decision turned on the absolute barrier against interstate commerce erected by Nebraska's reciprocity provision. *See also Hughes v. Oklahoma*, 441 U.S. 322 (1979).[9]

In sum, the absence of an absolute trade barrier in this case effectively distinguishes it from *Great Atlantic & Pacific Tea Co.* and *Sporhase*. Because Ohio has extended the tax credit to out-of-state producers of ethanol where their States grant a tax credit to Ohio producers, the statute does not discriminate against interstate commerce.

C. The Ohio Tax Credit Is Valid Under The Commerce Clause Because Commerce In Ethanol Owes Its Existence To Tax Incentives.

The Ohio tax credit is not, in any event, subject to Commerce Clause restraints because it is, in practical effect, a subsidy that has created the local and interstate market for ethanol. In *Hughes v. Alexandria Scrap Corp.*, 427 U.S. 794 (1976), this Court considered the constitutionality of a subsidy program enacted by the State of Maryland to rid the State of abandoned automobiles. Five years after the program was adopted, the statute was amended to make it more difficult for out-of-state processors to qualify for the subsidy. The Court rejected a Commerce Clause challenge by an out-of-state

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[9] *Hunt v. Washington Apple Advertising Comm'n*, 432 U.S. 333 (1977), upon which appellant relies (Brief 24, 26), is likewise inapposite. There, the Court struck down a North Carolina statute that required all out-of-state apples shipped into North Carolina to be sold under inferior federal grades or under no grades at all. In so holding, the Court observed that the North Carolina statute provided the State's apple industry the very sort of protection against out-of-state competition that the Commerce Clause was designed to prohibit (*id.* at 351-352). Here, on the other hand, it is undisputed that the Ohio reciprocal tax credit does not protect in-state ethanol producers from out-of-state competition but simply conditions the tax credit upon reciprocal treatment of Ohio-produced ethanol.

processor to the amended statute. The Court found "[n]othing in the purposes animating the Commerce Clause" to prohibit the State "from participating in the market and exercising the right to favor its own citizens over others" (*id.* at 810) (footnote omitted). The Court noted that "the commerce affected by the [challenged] amendment appears to have been created, in whole or in substantial part, by the Maryland bounty scheme" (*id.* at 809 n.18), and stated: "We would hesitate to hold that the Commerce Clause forbids state action reducing or eliminating a flow of commerce dependent for its existence upon state subsidy instead of private market forces" (*ibid.*). As Justice Stevens' concurring opinion explained, the Maryland subsidy "created a market that did not previously exist" (427 U.S. at 815) and which the State was not required to create "because the Commerce Clause surely does not impose on the States any obligation to subsidize out-of-state business" (*id.* at 815-816).

By subsidizing, through the tax credit, the production and sale of ethanol, Ohio has become a participant in the ethanol market. Since *Alexandria Scrap*, the Court has extended the State's market-participant immunity from Commerce Clause restrictions to contexts in which the commerce is not unique to the State. Freedom from Commerce Clause restraints has been recognized in the sale of commodities and in employment, commerce in which private parties also engage. In *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980), the Court upheld South Dakota's right to sell state-produced cement only to state residents, noting that "[t]he basic distinction drawn in *Alexandria Scrap* between States as market participants and States as market regulators makes good sense and sound law" (*id.* at 436). In *White v. Massachusetts Council of Construction Employers, Inc.*, 460 U.S. 204 (1983), the Court upheld the requirement of a work force of at least fifty percent city residents on all city-financed

or city-administered construction projects. The Court held that *Alexandria Scrap* and *Reeves* "stand for the proposition that when a state or local government enters the market as a participant it is not subject to the restraints of the Commerce Clause" (*id.* at 208).

This case does not require the Court to explore the limits of the State's immunity under the Commerce Clause when it acts as a market participant. This case is squarely controlled by *Alexandria Scrap*, for it is undisputed that commerce in ethanol would not exist without federal and state tax credits to gasoline dealers. The president of New Energy himself recognized that "absent those credits and ethanol would not be a viable factor in the market place today" (J.A. 65).

That this case involves a tax credit rather than a subsidy, as in *Alexandria Scrap*, does not serve to distinguish it. "Both tax exemptions and tax deductibility are a form of subsidy that is administered through the tax system." *Regan v. Taxation With Representation of Washington*, 461 U.S. 540, 544 (1983). As Justice Stevens explained in *Alexandria Scrap*, the Commerce Clause does not "inhibit a State's power to experiment with different methods of encouraging local industry[, w]hether the encouragement takes the form of a cash subsidy, a tax credit, or a special privilege . . . ." (426 U.S. at 816) (concurring opinion). *See also Arkansas Writers' Project, Inc. v. Ragland*, 107 S.Ct. 1722, 1730-1732 (1987) (Scalia, J., dissenting).

Alexandria Scrap teaches that a State's subsidy to commerce that it creates need not be exercised in favor of out-of-state businesses on the same terms as local businesses. *Alexandria Scrap* also teaches that the State does not lose the power to differentiate between in-state and out-of-state businesses by failing to make that distinction at the outset. The chronology of enacting a limitation—in that case, five years into the subsidy program—"does

not distinguish the case, for Commerce Clause purposes, from one in which a State offered bounties only to domestic producers from the start" (426 U.S. at 809) (footnote omitted). *See also id.* at 816 (Stevens, J., concurring).

Thus, *Alexandria Scrap* makes clear that Ohio's requirement of reciprocity as a condition of the ethanol tax credit is valid under the Commerce Clause as a limited subsidy; and the fact that New Energy can no longer take advantage of the credit previously available to it creates no constitutional infirmity. Ohio's "largesse" (426 U.S. at 809) prior to 1985 in providing an unconditional tax credit for ethanol was more than New Energy was constitutionally entitled to receive in a state-created market. Even the current law, which provides a tax credit to some out-of-state businesses, exceeds the requirements imposed by the Constitution on Ohio as a participant in the ethanol market. *Amici* submit that Ohio's role in creating the market for ethanol alone provides a basis for upholding the reciprocity requirement at issue in this case.

CONCLUSION

For the reasons stated, the judgment of the Supreme Court of Ohio should be affirmed.

Respectfully submitted,

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